

SUMMARY OF THE ADOPTED BUDGET

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GOVERNMENT FINANCE OFFICERS ASSOCIATION

*Distinguished
Budget Presentation
Award*

PRESENTED TO

**City of Baltimore
Maryland**

For the Fiscal Year Beginning

July 1, 2003

President

Executive Director

The Government Finance Officers Association of the United States and Canada (GFOA) presented a Distinguished Budget Presentation Award to the City of Baltimore, Maryland for its annual budget for the fiscal year beginning July 1, 2003.

In order to receive this award, a governmental unit must publish a budget document that meets program criteria as a policy document, as a financial plan, as an operations guide, and as a communication device.

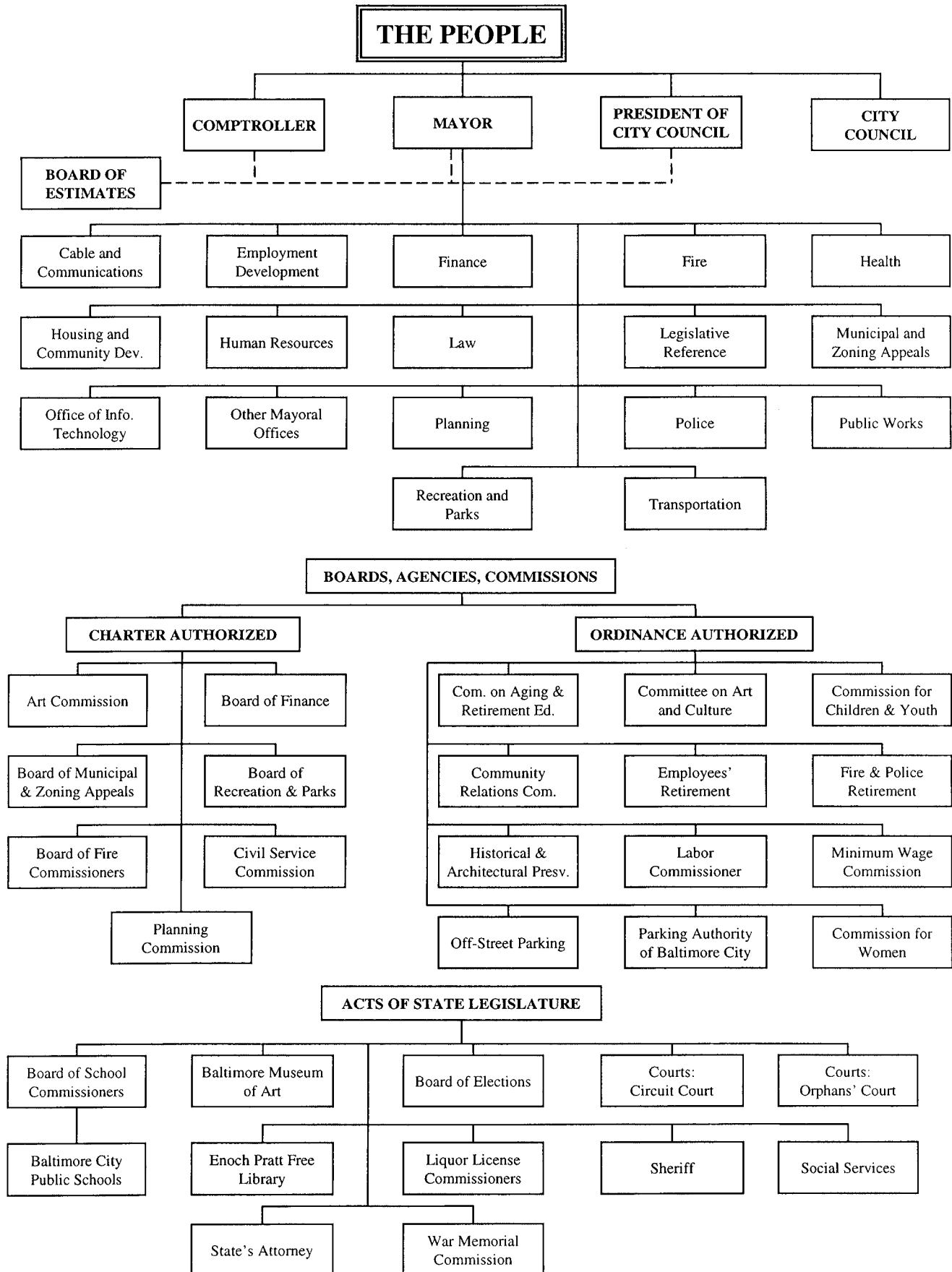
The award is valid for a period of one year only. We believe our current budget continues to conform to program requirements, and we are submitting it to GFOA to determine its eligibility for another award.

Fiscal 2005

Summary of the Adopted Budget

Budgetary Environment

MUNICIPAL ORGANIZATION CHART





Dear Taxpayer,

Thank you for investing in Baltimore. Because of you, our City has come a long way in the past four years. We have faced and met challenges. We have been confronted with and made difficult decisions. As a result of our hard work, together, we have made real and lasting progress.

Five years ago, Baltimore was the most addicted and violent city in America. Jay Leno was cracking jokes about our health problems. Property values were stagnant, and homes in all neighborhoods lingered on the market for months. Construction cranes and scaffolding were rare sights.

Today:

- Crime is at its lowest level since 1970 - leading America's big cities with a 37.0% reduction in violent crime from 1999 to 2003, according to the FBI.
- We are making strides against addiction - second only to Dallas in reducing drug-related emergency room admissions, according to the U.S. Department of Health and Human Services.
- Home values have nearly doubled from \$69,000 in 1999 to \$127,000 in May 2004 - with the number of home purchases up by 26.0% compared to last year.
- Currently, there is \$2.0 billion in new construction ongoing in neighborhoods throughout the City, and nearly \$2.0 billion more in the pipeline.
- And our children continue to achieve - with Maryland School Assessment scores rising in every grade - as we make the tough decisions necessary to fix the school system's financial problems.

Baltimore continues to face challenges. The lingering effect of the population and job loss of the '90s, and cuts from the State and federal government made this the most difficult budget year we have faced. We realized this was coming on the heels of a \$165.0 million State property tax increase, which is why we held the line on property and income taxes. By cutting more than 150 jobs (City-funded, non-public safety jobs are down from 9,552 in 1980 to 3,431 in 2004) and asking residents, nonprofits and businesses to pay a little more - while only increasing the budget at the rate of inflation - we will be able to continue our progress.

Thank you, again, for your faith in Baltimore. Our City, clearly, is becoming a better place to live. And I am committed to doing everything I can to protect your investment. If we continue to work together, and if we continue to believe, we will all benefit and our City will grow.

Sincerely,





MARTIN O'MALLEY
Mayor
250 City Hall
Baltimore, Maryland 21202

April 21, 2004

The Honorable Sheila Dixon, President
And Members of the City Council
City Hall, Room 400
Baltimore, Maryland 21202

RE: Fiscal 2005 Proposed Ordinance of Estimates

Dear Madam President and Council Members:

It is my duty and privilege to submit the Fiscal 2005 proposed Ordinance of Estimates. Together, our city has come a long way in the past four years. We have faced and met challenges. We have been confronted with and made difficult decisions. As a result of our hard work, we have made real and lasting progress.

In a time when our nation is at war, as we linger in a lengthy recession and a so-called "jobless recovery," and as more and more costs are being shifted to local government – including our nation's defense – this budget has proven to be the most difficult one we have faced.

Yet, despite these pressures, this budget is a reflection of our values as a city. It represents our best effort to continue our progress while recognizing the fiscal realities that limit city where the population – and tax base – declined by nearly 100,000 people during the last decade. This budget will ask for sacrifice from city workers, nonprofits and taxpayers. But will do so to advance our long-term goal of seeing our city grow, once again.

It is worth mentioning the progress we are working to protect:

- Baltimore has gone from the most violent big city in America to leading the nation in reducing violent crime over the past four years. Violent crime and overall crime are at their lowest levels since the 1960s – down 37.0% in 4 years. And the progress continues this year.
- Our increased investment in drug treatment, with the help of our State legislative delegation, has Baltimore second, behind only Dallas, in reducing drug-related emergency room admissions.

- Despite recent financial difficulties – which we are well on the way to resolving – our Schools’ students are improving test scores in every grade, with our students making the biggest improvements in the state in the most recent tests.
- As a result, home values have more than doubled in neighborhoods across the city. We have \$2.0 billion in new development underway in our city.

For years, because of our declining population and loss of jobs, our city put fiscal health at the center of everything we did:

- Our kids were getting arrested and dying, but we didn’t have any money, so we cut the Recreation and Parks’ budget in half.
- We were the most violent city in America, but we didn’t have any money, so we didn’t invest in public safety – or enough in drug treatment.
- We continually reduced our cleaning efforts.
- And a lack of funds became an all-purpose excuse for a lack of progress.

But if you don’t invest in growth... if you don’t invest in change, you just end up managing decline. And that’s what we did in Baltimore. Non-public safety city-funded employees have been cut from 9,500 to 3,500 since 1980. But it was not just employees that were cut - we reduced quality of life; we reduced our ability to grow as a city.

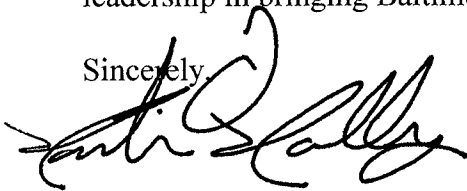
This year, we have a choice. The purpose of our revenue package is to maintain the improvements in quality of life – like crime reduction, increased cleanliness, and greater opportunities for children – that have resulted in increasing home values, new job opportunities and growth that will end Baltimore’s population loss.

Now, quality of life is at the center of everything we do. And growth is the long-term vision. Ultimately, growth – in population and jobs – is the way we begin to reduce our tax burden, not reducing basic city services. As we saw in the 1990s, no one invests in a city that’s dirty or dangerous.

We can either go back to managed decline. Or we can continue to invest in what is working. Look around our city. Are we better off now than we were 4 ½ years ago? We believe we’re not done yet. And we believe the citizens are willing to invest if they continue to see results.

Baltimore is a great American city – in my view the greatest. We still face many hard choices. We still have far to go. But today, we’re closer than we were yesterday. I am grateful for your leadership in bringing Baltimore back.

Sincerely,



Mayor

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SUMMARY OF THE ADOPTED BUDGET

Financial and Programmatic Policies

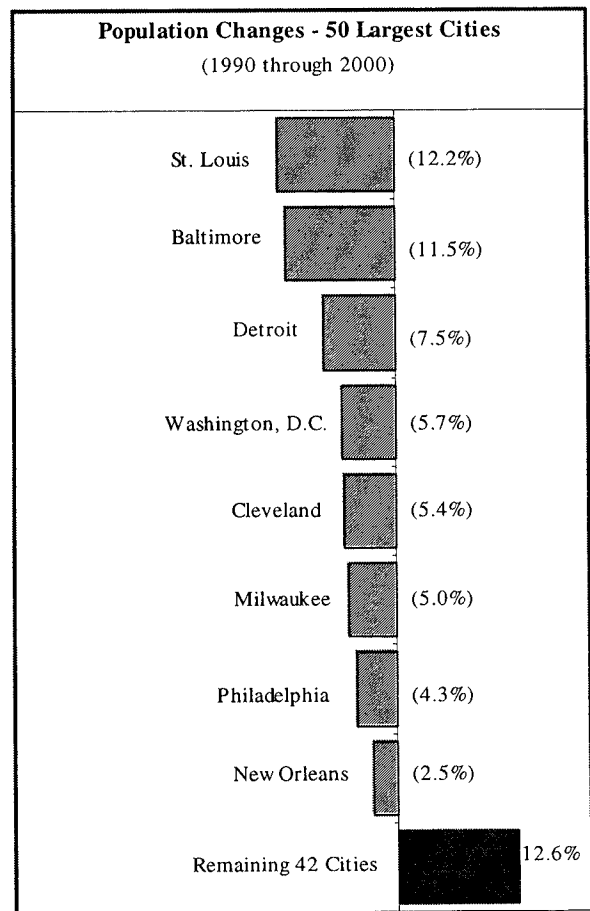
This section presents the four primary long-term concerns facing the City, enumerates the Mayor's primary objectives to address those concerns, and outlines the Fiscal 2005 budgetary actions to achieve those objectives. It also presents the major elements of the City's budgetary and related financial policies that provide for effective financial management to support work to achieve the Mayor's objectives.

LONG-TERM CONCERNS AND ISSUES

Population Loss - Much Less than Estimates Prior to 2000 Census

The 2000 Census documents a continuing decline in the City's population. The 2000 Census figure of 651,154 is substantially higher than the last population estimate prepared by the Census Bureau of 632,681 prior to the actual census. This may reflect a slowdown in migration from the City. It most certainly reflects dramatic changes in the number, size and composition of households making up Baltimore City. While the City lost substantial numbers of people, the decline in the number of households was much less, reflecting an influx of younger individuals and older childless couples.

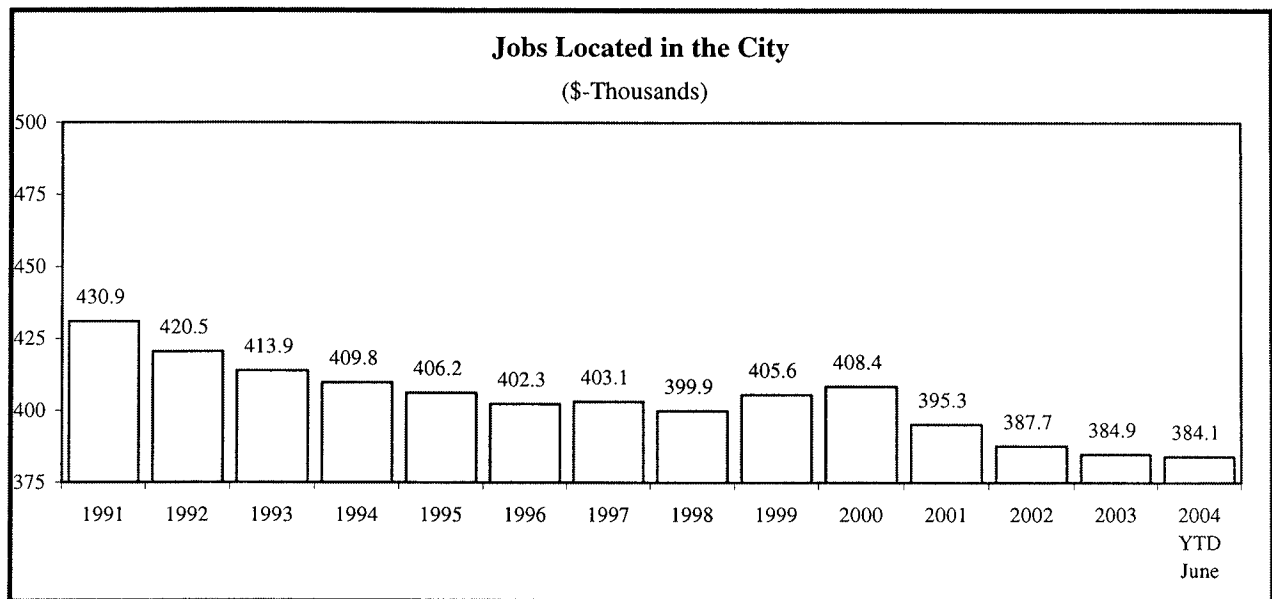
Marketing a city and changing perceptions held by people requires action. Actions must be taken to change the causes of negative perceptions. In addition, actions must be designed to serve the needs of this changing population profile. Changes are being made and are reflected in the budget priorities and programs that follow.



Job Loss - Though Tempered by the Attraction of New Employers and Retention and Expansion of Many Existing Employers - Must be Turned Around

The City needs to reverse the decline in its job base, which contributes to population loss. From its peak in 1991, the City has lost nearly 46,800 or about 10.9% of its jobs, while the rest of the State experienced about a 19.0% growth rate. The economic boom of the late 1990's contributed to job growth which peaked at about 408,400 in calendar 2000. Since that peak metropolitan

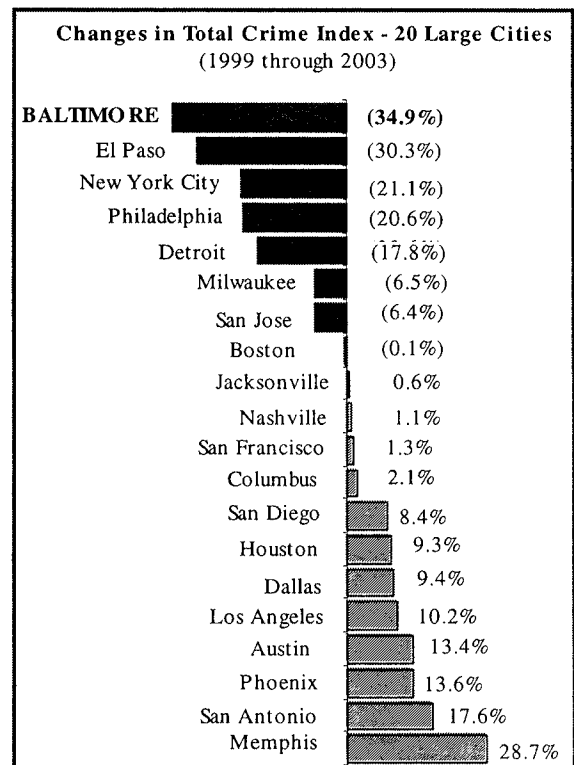
areas in the nation lost between 1 million and 2 million jobs. The most recent recession in the Calendar 2000 and 2001 period impacted Baltimore job growth materially.



Crime - Baltimore Leads Nation in Violent Crime Reduction – But Crime Rate Still Too High

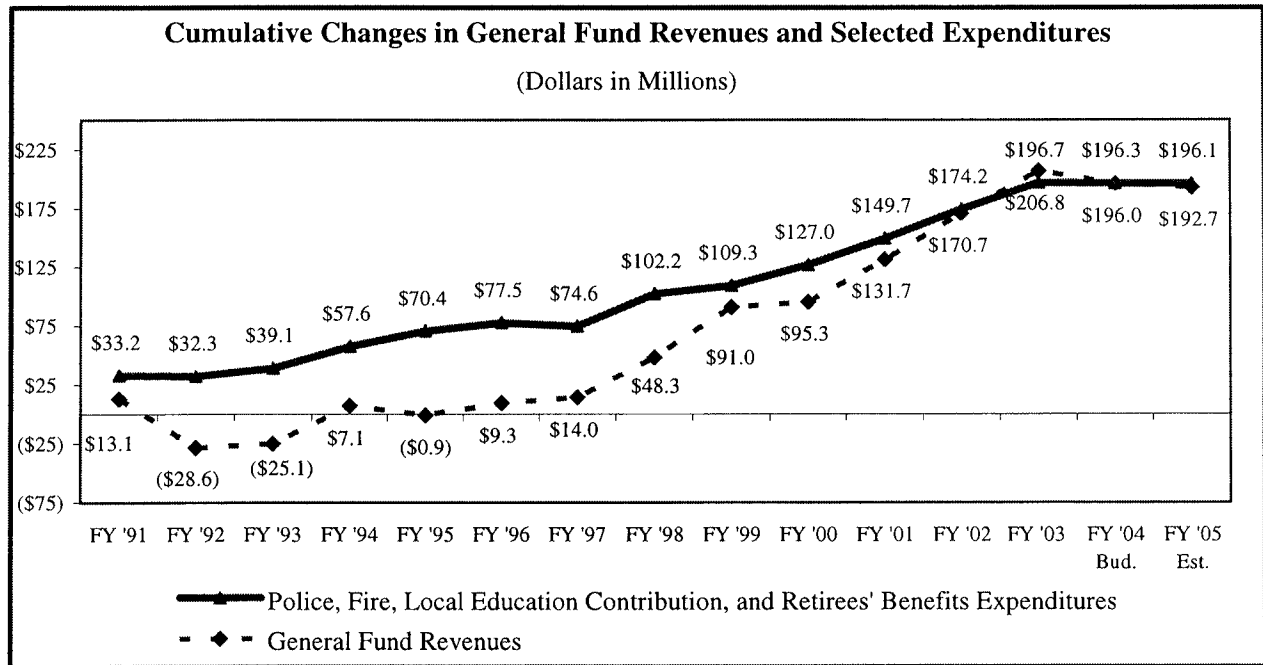
Baltimore budget priorities are driven by the concerns associated with the fear of crime. Making Baltimore a safe city is key to reversing the City's population and job loss. In the last three years, the number of murders in the City has been well below 300, a barrier that had not been broken for over a decade. Significant results are being realized from the City's investment to assure public safety.

Baltimore is transforming the image of being a dangerous large city. According to the most recent federal Uniform Crime Report, Baltimore led the 20 largest reporting cities with a reduction of 34.9% in total index crimes during the 1999 through 2003 period. A new generation of city dwellers is finding a home in America's central cities as fear of crime diminishes.



Budgetary Issues - Revenue Constraints and Expenditure Demands Persist Despite Record Levels of Real Estate Sales and Building Permit Revenues

Until such time as job and resident population growth are both turned around, the City will continue to labor under severe budgetary constraints. Growth in General Fund revenues has been inadequate to meet even a small portion of basic service needs. Over the past decade, General Fund revenue growth has been completely absorbed by spending needs in just three areas: public safety (police and fire), local contribution to the City school system and retired employees' benefits.



Despite successful past and continuing efforts to reduce and control spending, Baltimore remains a high tax city. High taxes result in part from the need to fund extraordinary services associated with being one of the poorest cities with some of the greatest service needs in the nation. These service needs must first be met to allow Baltimore to change its image and enhance investment opportunities. The City has in the last four and a half years made great advances in reducing violent crime and increasing drug treatment services. Challenges lay ahead that place enormous pressures on the City's limited resources.

CITYWIDE OBJECTIVES AND BUDGET ACTIONS

A clear statement of objectives is essential to guide competing agencies to most effectively use scarce resources to achieve their mission within the context of the Mayor's overall objectives and immediate priorities. The annual budget is the principal financial management tool for implementing changes to manage the structural deficit. As stated by the Mayor, the budget is a reflection of the community's values where "airy policy statements become concrete actions."

Based on the concerns cited above, the Mayor's primary objectives provide a guide for resolving the conflicts in allocating scarce budget resources. The objectives also serve as a clear direction in structuring the City's lobbying efforts to secure funding from the State and federal governments. Severe operating budget constraints mean that a large share of the initiatives

undertaken in this budget are either projects appropriated in the capital budget or projects funded as agencies re-engineer their limited resources to sustain basic services while squeezing resources to make room for initiating new activities. To sustain basic services in Fiscal 2005 required the enactment of a major new revenue package. See discussion in Section on Budget Adoption Related Budget Action. Within the constraints of the particularly severe funding limitations affecting the Fiscal 2005 budget, agencies were required to be particularly inventive to move forward on the Mayor's objectives.

Objective 1: Make Baltimore a safe, clean city

Changing the public perception about crime, safety and the scourge of drugs in the City requires budget actions. Improving performance in these areas is paramount. Homeland Security requirements impinge on this effort and compound the difficulty of the task as they take a prominent place in new spending plans, particularly in regard to safe-guarding the City and regional water supply system. The Fiscal 2005 budget plan supports the following actions to make Baltimore a safe and clean city:

- The General Fund continues to add support for police positions formerly funded by federal grants, absorbing 90 positions at a cost of \$4.6 million. The absorption of these grant funded positions highlights the importance given to public safety needs.
- The uniformed resources of the Police Department are continually redeployed to support drug enforcement activities of the Organized Crime Division. New strategies to provide a uniformed presence and follow up in neighborhoods to ensure drug trafficking cannot return after the departure of detectives will be implemented in Fiscal 2005. The budget provides funding for expansions of the pedestrian street lighting program.
- The Environmental Health unit will be joining enforcement efforts by implementing regulations and activities associated with the new Firearm and Ammunition Law and the effort to control firearms dealers because shootings continue to cause death among youth in Baltimore's poorest neighborhoods.
- The Capital Improvement Plan includes \$5.5 million for Homeland Security measures to provide protection to the Water and Waste water systems and lessen the vulnerability to outside influences. The Water and Waste water operating budget includes \$641,000 to support this objective.
- The Capital Plan includes \$23.0 million to convert to a safer means of disinfection by eliminating gaseous chlorine at each of the 15 chlorination facilities, including the Montebello Plants. Sodium hypochlorite will be substituted at an additional operating cost of \$1.7 million.
- The City will take the lead to secure proposals and develop a prescription drug discount card for use by all residents to lower health care costs and raise public health standards.
- The Fire Department is going to increase smoke detector installations by 10.0%.
- Working with the Police Department, the Mayor's Office of Information Technology will implement a pilot Closed Circuit Camera System program in the downtown West Side redevelopment project area. This program implements best practice found in Great Britain and elsewhere, that had material success in reducing crime through real time technology links to resource deployment decision makers.
- Dealing with drug addiction and achieving the most cost effective use of limited dollars to make drug treatment slots available is critical. Funding for treatment programs

administered by the Baltimore Substance Abuse System, Inc.(BSAS), the City's quasi-public, non profit corporation will flow directly to BSAS in Fiscal 2005.

- A new website will be developed by the Health Department to provide the public general information regarding the food inspection permit program, businesses the option of online permit renewal and helpful food tips for all users.
- To address HIV the Division of Maternal and Child Health will offer increased testing to cover 100.0% of its Adolescent and Reproductive Health clients with increased grant funding. The Health Department is also creating a Youth Health Advisory Board to increase involvement in planning, training and implementation of HIV/STD prevention services.
- The Department of Public Works will procure and install a state of the art Fuel Systems software package for the City's vehicle fleet that provides for effective fuel tank monitoring and tank leak detection.

Objective 2: Increase educational, cultural and recreational opportunities for children

Making the City safer and cleaner is a necessary starting point for securing and enhancing the opportunities for a child to live a full life. Beyond expanded program and funding initiatives outlined below to improve basic needs to support a healthy child appropriations are made to enhance cultural and recreation opportunities. Appropriations serving educational and cultural objectives for children in the Fiscal 2005 budget include the following:

- Total local funding from all funds for the public schools is \$207.6 million. The local share General Fund component at \$197.8 million exceeds the State-mandated Maintenance of Effort requirement by \$4.0 million and represents a per pupil funding increase.
- The City Health Department plans to increase the effectiveness of its nationally recognized Childhood Immunization program by increasing the immunization compliance rate from 99.7% in Fiscal 2004 to 99.9% in Fiscal 2005.
- School children in all 179 public schools will receive educational literature regarding nutrition and obesity. Weight reduction counseling and screening for hypertension and diabetes will be provide 80% of overweight children.
- All 15 school-based health centers will provide at least one tobacco prevention activity and 100.0% of students reporting tobacco use will receive counseling.
- The Department of Public Works Bureau of General Services is assisting the Public Schools with physical plant improvements at Benjamin Franklin Elementary, Diggs-Johnson Middle School, Edgecomb Circle Elementary, Gwynns Falls Elementary, and Eutaw-Marshall Elementary.
- The Department of Planning will join the Public Schools to rezone school districts for a better distribution of student population to improve class sizes and make more efficient use of buildings.
- The Fire Department will implement a new fire safety program in day care centers.
- The capital budget provides \$16.0 million in appropriations for Public School projects including: \$1.2 million for asbestos removal and general rehabilitation; \$6.5 million for renovation of two elementary schools; \$1.0 million of additional appropriation for replacement of one elementary school and \$7.3 million for renovation work at four high schools.

- The capital budget appropriates \$1.1 million for youth recreation center and athletic fields renovations as well as another \$4.9 million for park facilities used by children and adults.

Objective 3: Make government responsive, accountable and cost effective

Responsible public management requires the City to examine all options to operate in the most cost-effective manner while being responsive and accountable. Many of the initiatives involve the application of information technology to problem resolution. The Fiscal 2005 budget includes the following actions to serve this management objective.

- Fiscal 2005 will be the first full year of impact of changes in the City's health insurance cost sharing program involving increases in premium cost sharing, prescription and medical co-pay requirements. Calendar 2004 estimated savings amount to about \$18.0 million.
- The Department of Public Works will create a new Energy Conservation Office to reduce energy consumption and improve building systems. One position was created and six positions were transferred from other agency cost centers. The capital budget provides appropriation for energy efficiency and system replacement in various public buildings.
- Fleet Management in the Department of Public Works will utilize private contractors to improve efficiency, reduce energy costs and upgrade operational systems.
- Water and Waste Water will implement new deployment strategies to reduce overtime, unscheduled leave and accident time; decrease light duty roster; decrease work order backlogs; and improve average complaint resolution time.
- The Fiscal 2005 capital program includes \$500,000 to conduct a comprehensive audit of the water distribution system to reduce water loss, and \$24.9 million to rehabilitate 3.0 – 5.0% of the water distribution system annually to improve operational efficiency and reduce expense.
- The Automated Water Meter Reading Pilot Program will improve efficiency, maximize revenue, and ensure accurate metering of water usage. The use of hand-held meter reading devices will increase efficiency of water meter reading operations. In addition a study of the cost/benefit of privatization of meter reading will be undertaken.
- The Mayor's Office of Information Technology will implement a pilot program at the Enoch Pratt Free Library to test a private contractor's automated payroll time and attendance system. Like the real property tax system, this major information technology effort will replace a decades old legacy system badly in need of improvement.
- Animal control activities, including rat eradication and the removal of dead animals, previously in the Departments of Public Works and Transportation, are consolidated in the Health Department.
- The Commission on Historical and Architectural Preservation is moved to the reorganized Planning Department to improve efficiency of the permit review process and the creation of historic districts.
- To achieve potential savings associated with privatization, the Office of Homeless Services is established as a private entity, contracting with the Health Department to manage homeless grants and service programs on behalf of the City.
- The Bureau of Purchases in the Finance Department will implement a system to automate the submission and approval of requisitions, direct purchase orders and warehouse orders. The web-based system, called ComPASS, is currently in the prototype stage with City-wide roll out expected by the end of Calendar 2004.

- Fleet management will be improved as the Mayor's Office of Information Technology implements an Automatic Vehicle Location System through a Global Positioning System to track location, use status and availability. The Department of Public Works will procure and install a state of the art Fuel Systems software package for the vehicle fleet that provides for effective fuel tank monitoring and tank leak detection.

Objective 4: Strengthen Baltimore's economy by increasing the tax base, jobs and minority business opportunities

Increasing the tax base, jobs and business opportunities is the basis for the City's long-term prosperity. The City is expanding the use of Tax Increment Financing Districts first undertaken in Fiscal 2003, to support key development projects that provide jobs and stabilize neighborhoods. Working within the resource limits of the Fiscal 2005 budget, the following initiatives or expanded actions to strengthen the City's economy will be undertaken:

- The capital budget provides about \$21.0 million for major economic development projects.
- New general obligation bond and state grant funding of \$7.8 million is appropriated for the largest current economic development initiative, the West Side project, on the downtown district's western edge.
- The balance of new appropriations, approximately \$13.2 million, are provided for commercial and industrial park development, business corridor revitalization and brownfields site reclamation including funds for acquisition, loans and grants.
- For instance, a \$500,000 general obligation bond appropriation is provided for the stabilization of the Fayette Street Corridor stretching from downtown east to the Johns Hopkins medical campus and the East Baltimore Redevelopment project on the north side of the campus. This will support the City's investment of \$6.5 million of general obligation bonds and state funds to stabilize the neighborhood and create jobs north of the campus.
- The Bureau of Purchases is increasing participation for minority contractors by promoting informal bidding opportunities within the Construction Management Division.
- The Mayor's Office of Information Technology and other agencies will continue work on the third year of a multi-year contract to replace the City's outdated Property Tax Revenue System and provide improved timeliness in billing and improved cash flow.
- The Department of Planning will complete various neighborhood planning efforts including the Strategic Neighborhood Action Plans (SNAPS); Park Heights Community Plan, Coppin-Rosemont Community Plan, Westport/Middle Branch Master Plan, Coldstream-Homestead-Montebello (C-H-M) Neighborhood Plan, and the Pen Lucy Redevelopment Plan.
- The Fire Department plans to increase inspection activity and permit revenue by 5.0%.
- The Police Department will implement the first full year of the False Alarm Reduction program which will reduce and help offset the cost of police response to false alarms.
- The Department of Transportation capital budget provides about \$5.5 million for traffic signal related work to improve traffic flow and the City's viability as a business location. The project will use LED traffic signal technology to reduce operating and maintenance costs; provide for increased use of traffic surveillance cameras and improve traffic signal timing in order to optimize revenues from the red light camera program.

Objective 5: Create stable and healthy neighborhoods

In addition to the basic public safety tasks, including housing, building, fire and other code enforcement, the City must invest in creative efforts within fixed resources to stabilize and improve neighborhoods. This involves a major focus on abandoned properties, tax sale properties and other vacant and underutilized properties. The following Fiscal 2005 budget actions focus resources on neighborhood development.

- Fiscal 2005 capital appropriations for neighborhood development total \$54.2 million.
- The capital program includes a 50.0% appropriation increase to \$2.9 million for homeownership programs like the Live Near Your Work program and \$10.9 million in appropriation of General Obligation Bonds, Community Development Block Grant and other federal funds to support housing development, federal HOME funded projects and other projects at locations throughout the City.
- Building on success as the first city in the nation to have funding in place to demolish all high-rise low income public housing, the Fiscal 2005 capital appropriations provide \$5.4 million for infrastructure and other improvements at the new town home communities such as Flag House Courts.
- Over \$17.5 million in capital appropriation of General Obligation and state and federal funds is provided for acquisition, demolition, relocation, home repair and boarding programs to support the City's Project 5000 abandoned property program and the pioneering project to involved private sector realtors to market vacant properties.
- Federal grants for Homeless Services in the Department of Housing and Community Development are increased by \$1.5 million providing additional rental allowances for essential to support neighborhood stability.
- Three neighborhoods have been designated Federal Health Professional Shortage Areas and additional federal aid is provided to expand the function of two School Based Health Centers serving these neighborhoods. The centers will offer free health screenings and services to families of children enrolled in the schools.
- The annual tax sale is being used in more creative ways to put abandoned properties to use. The Finance Department will be building on the success of the sealed bid, bundled tax sale practice used in Fiscal 2004, by more fully utilizing the internet in the sale process and working with Water and Waste Water to identify appropriate properties to improve the tax sale process and increase bidder participation.
- The Department of Public Works will continue to implement an outsourced preventive maintenance program for rear load refuse packers to increase availability of equipment necessary to improve refuse collection in the neighborhoods.
- The Department of Public Works is improving abandoned vehicle storage and processing, a priority in order to rid neighborhoods of these blemishes, by working with the Mayor's Office of Information Technology to implement a new Tow Yard/Impound Information System. This system will replace a badly outdated legacy system in order to reduce property loss, move vehicles to auction faster and turn around use of scarce storage space.
- The capital budget provides \$750,000 in funding for the new Station North and Highland town neighborhood Arts and Entertainment districts and the older School #33 and Bromo Seltzer Tower art centers for studio and theater expansion and enhancement supporting the initiative to use arts and artists a major redevelopment tool.

KEY BUDGETARY AND FINANCIAL POLICIES

The establishment of clear objectives to align budget planning and ongoing agency operations to address the long-term issues and concerns confronting the City fails unless supported by sound fiscal management policies. This section presents major budgetary and financial policies that frame annual budget plan development and implementation. Many supporting policies (payroll, purchasing, retirement, etc.) are not summarized here.

Operating and Capital Budget Policies

Fundamental budget policies are set forth in the City Charter. See Budgetary Authority and Process - City Charter Provisions in Budget Process and Related Policies section.

Balanced Budget: The Charter requires a balanced budget. A difference between revenues and total expenditures is to be made up by adjusting the property tax rate or new revenues.

Public Hearings: The Charter mandates the Board of Estimates and the City Council conduct public hearings on the proposed budget.

Timely Adoption: The Charter schedule requires budget adoption before the fiscal year begins.

Budget Amendment: The Charter provides means for adopting supplemental appropriations funded from unanticipated revenues and/or new grants and sources that materialize during the year. The City's policy is to minimize the use of supplemental appropriations. In addition, the Charter allows for and spells out the procedures for amending the budget to transfer appropriations between programs within an agency and between agencies. See Fiscal 2004 Supplementary Appropriations in the Budget Process and Related Policies section for more information on budget amendments.

Budget Monitoring and Execution: Budget analysts maintain ongoing contact with agency fiscal officers in the process of implementation and execution of the budget. Expenditure and revenue projections are developed and reviewed on a monthly basis. The Mayor, through the Finance Department, exercises appropriate fiscal management to adjust budget policy as necessary to live within the limits of the current adopted plan. The City Council has the practice of reviewing budget performance at mid-year, during the budget development period in the fourth quarter and during the normal course of hearings on supplemental appropriations.

Six-Year Capital Plan: Guiding the physical development budget plan is the Charter requirement for a six-year capital improvement plan, the first year comprising the capital budget year. The plan is prepared in conformance with basic capital budgeting policies, which include appropriating funds in the year in which projects are likely to begin, financing a portion of capital improvements from current revenues and estimating the impact of capital projects on the operating budget. See Capital Plan budgetary Policy in Capital Budget section for more information on Capital Budget policies.

Financial Forecasting Policies

The City does three-year revenue and expenditure forecasts for governmental funds. The forecast is reviewed and updated at least twice a year. The multi-year forecast provides the basis for establishing budget targets and resource allocation to meet the Mayor's budget priorities.

Competitive Reengineering, Organization Redesign Policies

The ongoing effort to achieve cost reductions to fund operations within the limits of available revenue requires elimination of non-value added expenditures and other reductions in spending. Reductions have been achieved through a variety of means including the CitiStat program, consolidation and reorganization of agencies, staffing reductions through attrition and from time to time layoffs, privatization as appropriate, transfer of certain functions to the State and other methods. There has been a significant reduction of over 60.0% in General Fund staffing levels (exclusive of education, police and fire). This has resulted in a reduction in employees relative to the City's population. See the tables on Trends in Budgeted Personnel in the Fiscal 2005 Budget Plan section for staffing level trend details reflecting reengineering and cost containment effort.

Reserve Policies

Budget Stabilization Reserve: In 1993, the Budget Stabilization Reserve or Rainy Day Fund was established. The fund is designed to provide some General Fund budgetary flexibility should material funding shortfalls occur. Contributions are made as necessary to the fund in order to achieve and maintain a balance equal to at least 5.0% of General Fund revenues. The Budget Stabilization Fund had a \$56.2 million balance at June 30, 2003. The City continues to make annual contributions to the Budget Stabilization Reserve Fund. The Fiscal 2004 budget added \$800,000 to the Fund. The Fiscal 2005 budget appropriates another \$800,000 for the fund.

In Fiscal 2004 the City made a loan to the Baltimore City Public School System in the amount of \$42.0 million. To date, \$34.0 million has been repaid. The balance is due in Fiscal 2006. After taking account of repayment and anticipated contributions to the fund at the conclusion of Fiscal 2004 the fund is anticipated to meet the funding goal. The projected fund balance at the end of Fiscal 2004 is anticipated to meet the funding goal equal to 5.0% of General Fund revenues.

Undesignated Unreserved Fund Balance: The Charter places a limit on the size of the undesignated unreserved portion of the General Fund balance, requiring that any amount in excess of 1.0% of revenues be applied to reduce required capital borrowing. This restriction has placed the City in a relatively poor position compared to other large cities and works against the City's interest in achieving sound financial practices. The Charter permits only a small \$1.0 million annual contingency appropriation. With narrow reserve margins, it is essential for the City to have conservative budgeting estimates and plans. The preliminary Fiscal 2004 year end undesignated unreserved General fund balance is estimated to be about \$9.6 million.

Financial Reporting Policies

Budget, Accounting and Borrowing: The City has received the Government Finance Officers Association (GFOA) annual award for Excellence in Financial Reporting for over 20 years and the

Distinguished Budget Presentation award each year applied for since Fiscal 1988. The Consolidated Annual Financial Report is prepared in conformance with the Governmental Accounting Standards Board requirements. The City annually prepares the required full disclosure statements to comply with Securities and Exchange Commission requirements, provides fully descriptive notes in its annual financial report and disclosure statements and secures an unqualified independent audit report.

Debt Policies and Credit Rating

In 1990, the City adopted a formal debt policy which sets forth annual borrowing limits, consolidation of all financing arrangements within the Department of Finance, refunding and refinancing policies and limits on key debt management ratios. See Debt Service Overview section for detailed discussion. In the development of the annual borrowing plan, the effects of debt on key ratios outlined in the policy are updated and analyzed. The objective is to maintain the City's reputation in the credit rating community as having a conservative approach to all aspects of debt management including debt service expenses, debt retirement schedules and debt capacity ratios. The policy recognizes the fundamental role that debt has in the effort to maintain or improve the City's credit rating. The City's current credit ratings are A1 with Moody's, A+ with Fitch's and, A+ with Standard & Poor's. The City prepares an annual debt report, semi-annual multi-year debt service projections and periodic debt affordability analysis.

Cash Management and Investment Policies

The City's cash management and investment policy adopted in July 1995 covers investment objectives, types of investments, delegation of authority to invest, internal controls and reporting requirements. The City operates on a pooled cash basis and maintains a tiered portfolio containing a pyramid of investments with a long-term base and short-term top, in order to maximize and stabilize returns. The City has maintained a ratio of current assets to current liabilities greater than 1.0 since 1989 (a ratio of less than 1.0 being considered a fiscal stress warning sign).

Self-Insurance Policies

The City, through its Office of Risk Management, has a comprehensive program of risk exposure identification, evaluation, control and financing. The City is self-insured in the area of casualty and property losses, including the uninsured portion of City buildings and contents, workers' compensation and employers' liability, employees' health insurance, third party general liability and automobile liability losses. To the extent possible, the City plans to address concerns about risk management reserves by making additional appropriations and by adjusting agency premiums to help provide adequate funding.

Fiscal Policies for Economic Development

The Comprehensive Economic Development Strategy plan submitted to the State in 1999 sets forth economic development goals, objectives and priorities. This plan was consistent with "PlanBaltimore," the comprehensive master plan for the City's development over the next 20

years, prepared in 1999. A primary goal of the economic development plan is to attract more job generating businesses to the City. To that end, the City has developed a variety of development incentives including loans and grants. In the last 10 years the City has expanded the incentives to include tax incentive programs. The budget plan estimates and reports on one type of tax expenditure, property tax credits. The budget document also contains legislatively mandated cost and benefit analysis on tax credit programs (see Summary of Tax Expenditure discussion and City Real Property Tax Credit Programs in the Revenue Outlook Section for property tax credit expenditure program descriptions). The City is committed to perform consistent and thorough analysis of the cost and benefit of its growing package of incentive programs.

Fiscal Stability Policies

One-Time Revenues/One-Time Expenditure Savings: The City policy is to use one-time windfall revenues and expenditure savings for one-time expenses. For instance, the Fiscal 2004 budget plan uses a portion of fund balance, generated in substantial part in Fiscal 2002 and 2003 to fund one-time expenditure requirements.

Short Term Borrowing: The City Charter prohibits the creation of any short term debt to finance current budgetary operations except for the issuance of tax/revenue anticipation notes to be redeemed in the same fiscal period.

Employee and Retiree Benefits Program Costs: Because total employee compensation costs are the largest share of the City's expenses, it is absolutely essential that options to control costs of employee benefits be examined. The City has an ongoing joint labor-management Health Insurance Committee. Certain recommendations made by the committee are subject to bargaining processes with employee groups. The City, working with the privately funded Baltimore Economy and Efficiency Foundation, cosponsored a comparative benefits study to make recommendations to control these expenses. The recommendations are currently under review by the committee.

Lobby for Increased State Aid: Special needs as an historic urban center require an ongoing lobbying program for increased State Aid targeted particularly for the school system, courts, crime reduction efforts, substance abuse treatment and economic development programs.

Budget Emergencies: The City Charter provides a mechanism for the Finance Department, under guidelines approved by the Board of Estimates, to establish expenditure schedules or strict budgetary allotments when warranted by financial conditions. In addition, the City Charter permits the budget to include up to \$1.0 million in General Fund appropriations as a contingent fund for emergencies.

Assumption of Grant Program Costs: The City's general policy is to terminate grant programs when federal and State funding is terminated. In recent years, limited exceptions to this policy have been made. In the area of crime fighting and prosecution of crime, the City General Fund has absorbed certain grant expenses in the Courts, State's Attorney and Police agencies.

FISCAL 2005 SHORT-TERM BUDGET POLICY AND PREPARATION GUIDELINES

Development and review of the Fiscal 2005 budget requests were conducted in the context of the most severe spending reduction targets due to the narrow local tax base and local resource limitations. Adoption of a major revenue base expansion program was necessary to maintain basic City services. See discussion in Section entitled Post Budget Adoption actions. Agencies received the following policy guidelines for use in the construction of their Fiscal 2005 budgets:

Local Revenue Constraints – The budget guidelines restated the structural deficit projection problem and the priority to be given to public safety spending.

Targets – Agencies were given target levels to build budgets reflecting resource limitations.

Cost Reductions/Expenses to Meet Targets – Agencies were instructed to eliminate all costs associated with position abolishment required to meet targets. Since salary savings were not to be increased to meet the required budget target level, positions had to be abolished.

Competitive Reengineering/Privatization – Agencies were encouraged to develop additional plans for use of private sources to achieve budgetary cost savings.

Elimination of Grant Programs – With the exception of federal funding for additional police officers, where grants require the City to phase in local support for additional police personnel, agencies were instructed to phase-out programs where grant funding was terminated.

Fleet and Fringe Benefits Charges – Agencies were instructed to maintain prior year budget levels for fleet costs. Fringe benefit costs factors were developed for agencies.

General Fund Personnel Freeze – Agencies were directed to abolish General Fund positions equal in number to any requests for new positions.

OTHER FINANCIAL POLICIES AND PRACTICES

Development of the annual budget plan is guided as well by other policies and practices set forth in the City Charter, federal, State and local law, action of the Board of Estimates, procedures established for budget planning, implementation and control and related accounting practices. Policies and practices are discussed in the following sections of this document.

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